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The Corporate Perspective

by John Hein
Director, International Economics

The Conference Board

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THE CONFERENCE BOARD, INC.
845 Third Avenue, New York, N.Y. 10022
THE CONFERENCE BOARD OF CANADA
25 McArthur Road, Ottawa, Ontario, K1L-6R3, Canada
THE CONFERENCE BOARD INC.
Avenue Louise, 207 Bte 5, B-1050 Brussels, Belgium

THIS REPORT, the seventh of its kind, is based on material submitted by a panel of economists, planners and analysts in U.S. private industry. As in previous years, the panel members were asked by The Conference Board for their assessment of economic conditions abroad during the coming year, particularly in countries "that are important to your company's foreign operations or on which you normally gather information."

The report is based on the replies received from panelists in 12 major business organizations. Eight of these are among the 250 largest U.S. industrial corporations as listed by *Fortune;* two each are in the financial and transportation sectors. Most of the material submitted was prepared between early July and early September.

The Conference Board believes that this kind of survey is valuable, since corporate assessments are important in determining the level and mix of capital expenditures, marketing programs, and production schedules for the companies' international activities. Indeed, as one of the panelists pointed out, his data and assumptions "are intended to serve as guidelines for planning" in the period immediately ahead. But the material "will be useful not only to planning departments, but also to other departments such as purchasing, pricing and marketing, where general economic conditions have a major impact."

The material does, in fact, represent a great variety of opinions and forecasting styles—from hunch and pure judgment to rather elaborate, computer-based forecasts. But it is worth stressing that the data, prepared as they are for internal corporate use, are not predictions, but merely estimates of the ranges within which certain parameters might fall in the near term. As one panel member noted, the material spells out "what we regard as the most likely course" for the various economies and for financial markets through the company's planning period.

Thus, as someone had pointed out in a previous survey, the estimates represent the mean results of the possible paths foreign economies might follow in the absence of major shocks or disruptions. Still, the projections may be read and interpreted differently, depending on the user's corporate function or industrial sector. According to one panel member: "The high degree of uncertainty in the outlook and disparity of dissenting views among economists underscores the need for each division to evaluate the impact of alternate economic scenarios on its particular business. For each division the relative impact will vary according to geographic commitments and industry sectors served."

General Overview

In its midyear economic review, released last July, the Organization for Economic Cooperation and Development (OECD), which encompasses the 24 major industrial countries, noted: "The influences now acting upon OECD economies are diverse, and are moving countries into somewhat different cyclical phases. A recovery in activity is thought to be occuring currently in Europe and Japan, and one is expected in North America in the second half of this year." But, the review noted, "there will probably be important differences between the United States, Japan and Europe," with gross national product (GNP) growing by little more than 2 percent next year in the United States, by 2½ percent in Europe, and by slightly under 4 percent in Japan (see Table 1).

The Conference Board's *International Economic Scoreboard* commented in a similar vein in August that "prospects for recovery from the world recession are more promising in Europe and Japan than in the U.S. and Canada, according to the most recent data for the leading indicators."It therefore saw world recovery hinging on "the development of an upswing in the U.S. and Canada, which is still problematical." In October, the *Scoreboard* noted further declines in the indexes for the United States and Japan, while "smaller declines in France and Italy and continued stagnation in Canada make the world picture more somber than it was two months ago" (see Chart 1).

The panel shared this generally cautious view about economic recovery in the major industrial countries, although there were some noticeable differences of opinion about both the stimuli to and the strength of business activity in the year ahead. Much was seen as depending on developments in the United States. "Gradual improvement in economic activity," one panelist writes, "is expected to become evident during the second half of 1982, based on modest gains in consumer spending, inventory replenishment, and increasing ex-

Table 1: Official Growth and Inflation Forecast (Percentage changes at annual rates)

	From previous year		From previous half year		
	1982	1983	1982	1983	
Growth Real GNP			Second half	First half	Second half
United States	— 1.5	2.25	2.0	2.0	2.75
Canada	— 1.75	1.0	— 1.5	1.75	2.25
Japan	2.0	4.0	3.0	4.0	4.75
France	2.25	2.5	3.0	2.25	2.25
Germany	1.0	3.25	2.0	3.5	3.75
Italy	1.5	2.5	2.5	2.75	2.75
United Kingdom	1.25	1.75	2.0	1.5	1.75
All seven countries	0.25	2.5	2.25	2.5	3.0
Other OECD countries	1.5	2.5	2.0	2.5	2.5
Total OECD	0.5	2.5	2.25	2.5	3.0
GNP Deflators					
United States	6.0	5.5	5.0	5.75	6.0
Canada	10.5	10.0	10.0	9.75	10.0
Japan	3.5	3.75	3.25	4.25	3.5
France	13.75	13.75	13.5	14.0	13.0
Germany	4.25	2.75	3.0	2.5	2.5
Italy	15.5	15.0	15.5	15.0	14.5
United Kingdom	8.5	7.5	7.75	7.75	6.75
All seven countries	7.25	7.0	6.5	7.0	7.0
Other OECD countries	11.25	10.5	11.0	10.25	10.0
Total OECD	8.0	7.5	7.25	7.5	7.5

Source: Organization for Economic Cooperation and Development, *Economic Outlook*, July, 1982.

ports for the major industrial countries." But continued growth of economic activity outside the United States next year is "contingent upon some further easing in the real cost of credit and recovery in the U.S. economy."

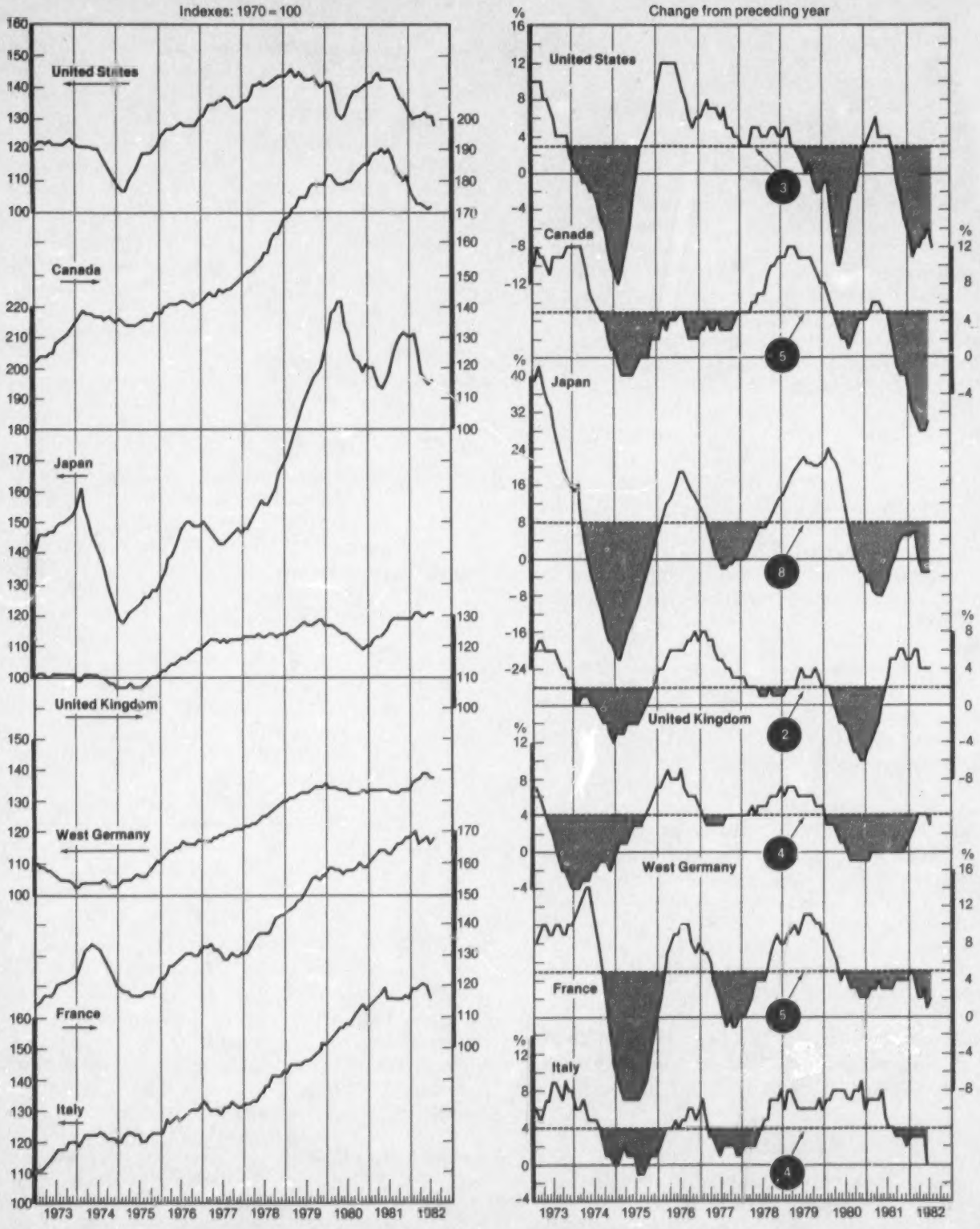
At the same time, however: "It is not inconceivable that some countries, despite much public posturing against 'exaggerated' dollar strength, are in fact not too unhappy at the de facto devaluation that helps their export industries." And: "I am fairly sure that U.S. imports would be much weaker if the dollar were not so strong. We expect a lot of pickup in imports next year because of the dollar despite our poor outlook for the U.S. economy."

Another correspondent casts his net wider. "Economic data continue to confirm the beginnings of recovery in Europe and the bottoming-out of the recession in North America. But tight monetary policy and high interest rates in the United States have kept the pace of the recovery slow by historical standards and will perpetuate the continued rise of unemployment for some time to come. The smaller OECD countries and the newly industrializing economies of the Pacific and Latin America will have to wait until late this year or early 1983 before demand from the larger countries of Europe and the United States begins to pull their economies out of recession."

But any eventual recovery will be modest, by historical standards, according to most panelists, with growth constrained by forces affecting all components of business activity. One panelist examines these forces in some detail.

> "Personal consumption expenditures will remain constrained by the sluggishness of real income growth throughout the OECD. After rising by 1.3 percent in 1981, real wages are projected to increase by no more than 1 to 1¼ percent in 1982, and by a similar percentage during 1983. Absolute declines in real wages are estimated in a number of countries in 1982, notably in Belgium, Norway, Ireland and Sweden.
>
> "Private-sector investment should reflect the completion of inventory liquidation, but outlays for plant and equipment will show little growth in light of their high opportunity cost relative to positive real returns or riskless and liquid financial assets. Government expenditures are projected to decline as a percentage of GNP as a conscious policy decision everywhere except in France, Italy and, conceivably, Japan, as the inflationary

Chart 1: Leading Business Cycle Indexes



Source: *International Economic Scoreboard*, The Conference Board, October, 1982.

effects of deficit spending have come to be better appreciated.

"There is a lingering hope that exports could provide the needed impetus, but this has always struck us as wishful thinking in view of the subdued worldwide growth environment, including prospects for an anemic recovery in the United States and the relentless Japanese export drive. It is interesting to note that even German export orders have recently been faltering despite the weakness of the Deutsche mark."

A second dissenting voice was heard: "Our U.S. outlook is considerably different from the consensus. We expect that this will have an impact on foreign economies, particularly those in Europe. Specifically, we are expecting a renewal of recessionary forces in the second and third quarters of 1983. We expect the U.S. economy to expand fairly strongly in the fourth quarter of this year and the first quarter of next year, but then to succumb to another decline as U.S. interest rates rise once again. This interest rate scenario will flow through Europe, causing a very weak second and third quarter in 1983."

Others, however, were somewhat more optimistic and detected some basic forces that, in the longer run, could put the world economy onto a more sustainable footing. "As 1982 progresses," one panelist notes, "the basis for a return to stability could be evolving through a convergence of the U.S., German and Japanese economies. To the extent that these leading industrial nations curb inflation and follow similar economic courses, the principal cause of volatility among their currencies would be much reduced. The emergence of less inflation, lower interest rates, and moderately stable exchange rates among the 'big three' would then contribute to more general world economic stability and greater prosperity in the 1980's."

One panel member, finally, detected even more hopeful signs amidst the general outlook. "There has been some fundamental and permanent improvement in inflation trends. The current weakness of world commodity prices is a factor in the improved inflation outlook. The declining price of oil, which looms so large in every country's economy, has been particularly favorable. There is major uncertainty about future oil prices. Governments of industrialized countries are attempting to stimulate investment growth. The policies which have had such painful repercussions for business in the short term are likely to create the foundation for a period of satisfactory growth later on."

Major Industrial Countries

The panel's assessment of the outlook for individual foreign countries generally pointed in the same direction, especially for Western Europe, Canada and Japan; there was slightly more variation for non-European countries (see Table 2). Of course, "improvement" or "better performance" for GNP and the inflation rate may not amount to very much if the relevant changes are small, or if growth this year has been zero or negative and inflation has been rampant.

Even where improvement in inflation and the rates of growth are foreseen, there still may be differing views as to the actual numbers for individual countries. Some of these projections for the major industrial countries are shown in Chart 2, in order to illustrate the range of "the most likely course" anticipated by panel members.

In discussing its annual report for 1981, optimistically entitled "Room for Maneuver," the Economic Council of *Canada* noted: "Canada's economic problems may not be as stubborn and unmanageable as everyone had thought. It now looks as if the federal government could develop effective policies to deal with the legacy of the 1970's and get the country back on a better growth path again. And it may even be possible to make more headway in the war against inflation if monetary policy does not have to fight the good fight all on its own."

For the short term, however, the outlook is considerably more restrained. The Conference Board of Canada forecasts only a relatively weak recovery in 1983, with GNP growth of 2.2 percent as against this year's 0.2 percent. Underlying this projection is the assumption that while interest rates may fall somewhat in the second half of this year, they will still remain high in 1983, with a continued dampening effect on the economy. Nor will the battle against inflation show overly impressive results. Following a double-digit increase (10.2 percent) this year, consumer prices are expected to rise by around 8 percent in 1983. This would reflect lower prices of imports from the United States (with further inroads by U.S. products into sensitive Canadian sectors), lower food prices, and adjustment of Canadian oil prices to more realistic levels. Wage settlements are expected to contribute little to the abatement of inflation.

The U.S. connection also emerges strongly in the views of several panelists. One notes succinctly: "The Canadian economy is strongly affected by developments in the U.S. economy, especially as regards the overall business cycle which is interconnected through U.S. export market and financial policies."

Another elaborates further: "In Canada, the depressed U.S. motor vehicle and housing sectors have precipitated a recession more severe than in the United States. Also contributing to the decline has been a Canadian energy policy that has discouraged investment in oil exploration and production activities, particularly on the part of foreign firms. In fact, foreign investment in general has been discouraged in an attempt to 'Canadianize' the ownerships of basic industries. Since foreign capital inflows have played such an important role in the Canadian economy in the past, the lack of these inflows

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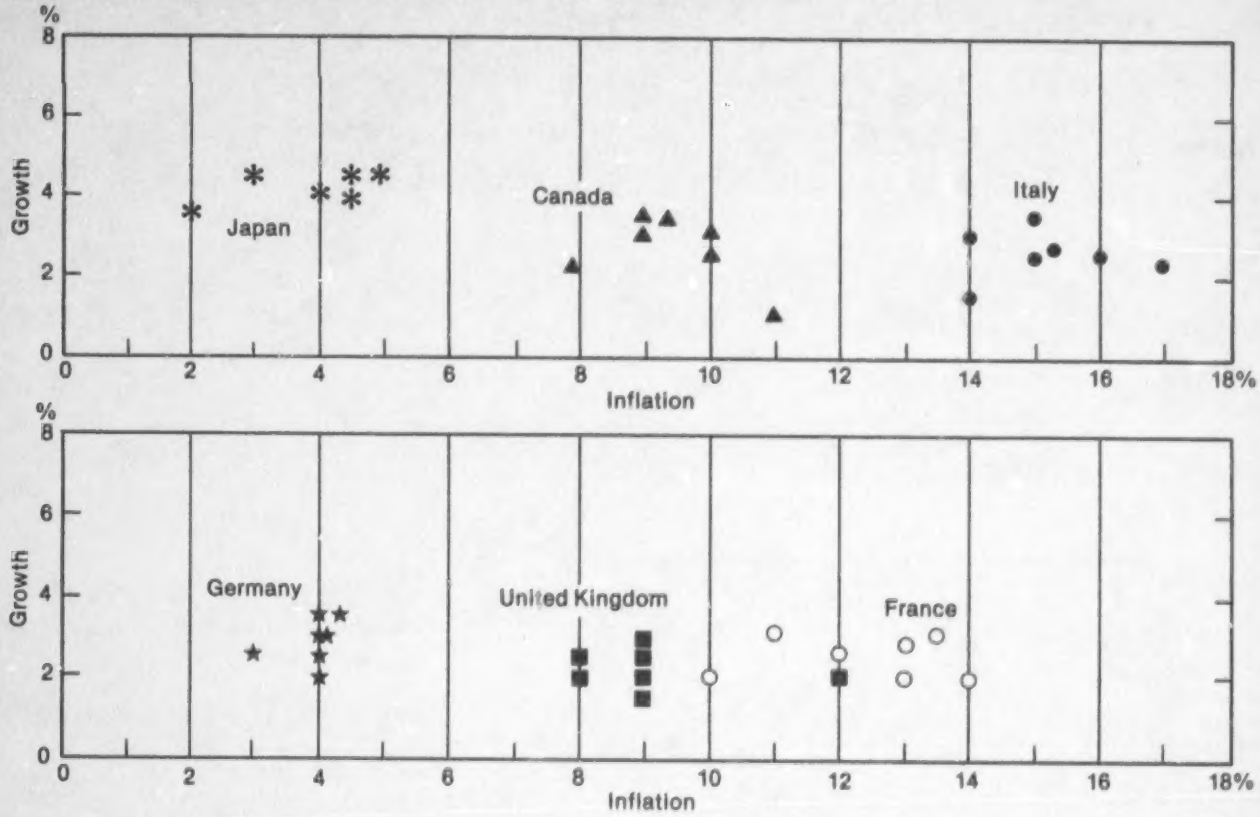
Table 2: The Corporate Outlook (1983 as compared to 1982))
Note: Each entry represents the 1983 forecast of an individual panelist.

	Growth			Inflation		
	Higher	*Same*[1]	*Lower*	*Lower*	*Same*[1]	*Higher*
United States	xxxxx xx			x	xxxxx	x
Canada	xxxxx xxx			xxxxx xx		x
Japan	xxxxx xxxx	x		x	xxxxx xxxx	
France	xxxx	xxxxx x		xxxxx x	xxxx	
Germany	xxxxx xxxxx			xxxxx xxx	xx	
Italy	xxxxx xxxx			xxxxx xx	xx	
United Kingdom	xxxxx xxxx	x		xxxxx xxx	x	x
Austria		xx		x	x	
Belgium	xxxxx xxx			xxxxx xxx		
Netherlands	xxxxx xxx	x		xxxx	xxxx	x
Spain	xxxx	x		xxxx	x	
Sweden	xxx			xx	x	
Switzerland	xxxx			xx	xx	
Argentina	xxxxx x			xxxx		xx
Australia	xx	xxxx	xx	xxx	xxxx	x
Brazil	xxxxx x	xx		xxxxx xxx		
Hong Kong	xxxx	xx		xxxxx	x	
Korea	xxxxx x			xxxx		xx
Mexico	xxxxx	xxxx		xxxxx x	xxx	
Singapore	xxxx			xxx	x	
South Africa		x		x		
Taiwan	xxx	x		xxxx		
Venezuela	xx	x			x	xx

Chart 2: Growth and Inflation in Six Countries: Forecasts for 1983



Observations represent forecasts for growth and inflation rates in 1983 submitted by individual panelists.

is expected to have an adverse effect on both internal economic performance and the value of the Canadian dollar through 1983."

The often-noted discrepancies between federal and provincial policies prompted these comments: "The fragmented nature of the Canadian market will present increasing problems for firms with operations scattered across the country. With a mere 10 percent of the work force subject to federal standards on labor, companies will observe a wide variety of provincial rules that will mean widening discrepancies in wage rates and other conditions from province to province. Labor costs will be 10 to 20 percent higher in Western Canada due to overheated growth in the region's resource-led economies."

Easily the most gloomy assessment of Canada's prospects comes from a panel member to whom the expected modest recovery in 1983 means that "by the end of next year, real GNP would be only about flat with its 1980 and 1981 levels. This is poor in itself, but is even worse in comparison to the United States." He continues:

"Even with a lowering of interest rates in the United States, upward pressure could remain on Canadian rates, given an estimated C$19.6 billion federal government budget deficit (about 5.5 percent of GNP) and the estimated 11 percent inflation rate. We would, therefore, expect little help from the business sector in pulling the economy out of recession. Corporate liquidity is dangerously low; profits declined some 44 percent in this year's first quarter from year-ago levels. With penuriously high interest rates (which helped interest payments soak up some 60 percent of corporate profits in the first quarter) and operating rates below 70 percent overall (and nearer 50 percent in some sectors), the Canadian businessman will be hard put to justify any capital spending that does not add immediately to cash flow. Nor would we expect the Canadian consumer to pick up the ball. Though apparently better able to do so than the businessmen (13 percent savings rate and real wage gains for the first time in several years), consumers have little or no confidence in the economy (or Ottawa's ability to manage it). Finally, with only weak recovery expected worldwide from severe recession, we would not expect the export markets to do much to spur the Canadian economy over the near term."

In *Japan*, pressures have been building up for the government to take measures to reflate the economy. Indeed, those who advocate a large budget deficit to stimulate economic activity argue that it would also serve to strengthen the yen, by putting upward pressure on domestic interest rates and thus narrowing the gap between Japanese and U.S. rates. Others contend that higher rates would simply raise the cost of running a deficit. The first group, the expansionists, led by the Economic Planning Agency and the Japan Economic Research Center, aim at boosting growth in the fiscal year ending in March, 1984, to over 4 percent. The other group, the budget balancers, identified largely with Japanese industry, insist that priority be given to spending cuts despite the continuing recession.

While these issues are being debated, Japan generally is expected to do reasonably well in 1983 compared with the other industrial countries. Although to one panelist the growth anticipated for next year looks "paltry compared with Japan's experience during the early 1970's, it will still be the highest GNP real growth rate of any OECD country." But, he notes, "to achieve even this forecast will not be an easy task, as the country can no longer rely upon the export sector providing most of the thrust. Export growth will probably be held to a single-digit number around 5 percent."

Another panel member writes:

> "A slower economic recovery may force the government to reexamine its basic strategy of seeking fiscal stability at the expense of growth. However, what the government can do to stimulate the economy is limited, since continued reliance on export growth must be avoided in view of the growing trade frictions. To increase public-works spending or reduce income taxes would lead to a widening of the budget deficit—and Suzuki has already announced his aim to balance the budget by fiscal 1984.
>
> "A third possible way to stimulate domestic growth—by lowering the interest rate—is a remote possibility because it is already low (the banking discount rate is at 5.5 percent), and a further cut could adversely affect the yen exchange rate.
>
> "With an average annual growth of 4.5 percent anticipated for the next five years, and a per capita income exceeding $8,000, the sixth most populous country is among the richest markets in the world. Opportunities for MNC's, however, will continue to be severely constricted by the fiercely competitive domestic market, high cost of market entry, and the government-industry determination to strengthen the position of Japanese companies against foreign firms in domestic markets."

Japan's dependence on exports, and hence on recovery of economic activity elsewhere, is stressed by other respondents. "The outlook for the Japanese economy remains hinged to the economic performance of the rest of the world. If the recoveries in the United States and Europe are weaker than expected, or if protectionist actions increase the barriers to Japanese exports, economic growth could be lower than the current forecast." "Assuming the anticipated acceleration of economic activity in other world economies, Japan's growth should increase to about 4 percent for 1983."

But no discussion of Japan can avoid the issue of the country's export competitiveness and the resulting large trade surplus. "The continuing large Japanese trade surpluses, especially with the United States, are intensifying the debate on trade issues. Yet the Japanese have still not made any significant moves to open their markets to imports."

"Trade friction with other countries continues to be a major issue and, in May, the government unveiled a second package of trade measures following the West's lukewarm response to the January reduction on nontariff barriers. The focus of attention is now on the liberalization of agricultural imports, a request of the U.S. government that is bitterly opposed by farm groups in Japan. As presently planned, tariffs on a variety of industrial goods will be reduced or eliminated by April, 1983, but only a few items will have their import quotas increased."

It is encouraging to find that these issues are recognized in Japan as well, and that broad-based solutions are at least being discussed among some of the "expansionists" (see box on page 10).

France's Economic and Finance Minister Jacques Delors reportedly declared last March—at a time when the franc was under attack—that "all the objective elements of the economy are satisfactory." Most observers would tend to disagree with that statement. Indeed, after wages were frozen and the franc was devalued last summer, *The Economist* was prompted to proclaim that "Socialist France's bold economic experiment has failed."

What are the facts? In adopting an austerity program, President Mitterand abandoned the high-spending policy that he had hoped would cope with unemployment. His only consolation is that unemployment in France grew more slowly over the year through last June than elsewhere in Europe. Consumer demand, which rose by 6 percent over a year earlier during the Socialists' first nine months in office, began to falter subsequently. While demand was initially buoyed by large wage increases for lower paid workers and hefty social-security increases, the wage freeze imposed last June spelled a drop in living standards for most French people.

Investment by the public sector has failed to increase in real terms, and the government's hopes that some of the newly nationalized companies could serve as "motors" for the entire economy have proven false. Private-sector investment likewise fell in both 1981 and this year. In-

Japan and the World Economy

"The maintenance of the growth vitality of the Japanese economy is also essential in relation to the revitalization of the world economy. The time when the 'success of a summit' was measured by the fact that 'Japan was not criticized' should have passed long ago. Thus, in order to find appropriate ways to get the world economy back on the right track, a more positive Japanese attitude is called for, i.e., an attitude based on the awareness that Japan is the second largest economy of the free world, and not one based on the hitherto prevailing 'victims' mentality' pointed out above. In that sense, to take the advocacy of a domestic demand expansion policy as an example, it does not mean that, if there is no severe external criticism, there is no need to carry it through. Also, Japan ought to have stood in line with Europe in sternly insisting on the rectification of the high U.S. interest rates. Of course, it might be unreasonable to expect any substantial results from a summit meeting alone. Thus, for the sake of the revitalization of the world economy, the pursuit of solutions to outstanding economic problems, such as rectification of high U.S. interest rates, prevention of protectionist measures in various countries, liberalization of the Japanese market, and expansion of domestic demand, must be an ongoing process—and not just topics to be considered on the occasion of summit meetings. The finding of solutions to these problems is not only important for the industrialized countries, but also vital to the surrounding developing countries which are presently confronted with the threat of stagnating economies."

Quarterly Forecast of Japan's Economy,
The Japan Economic Research Center, June, 1982.

deed, despite valiant government efforts to allay the fears of the business community, the government has encountered considerable resistance in securing the active cooperation of the French Employers' Association and, in addition, has seen a marked dropping off in the plans of foreign companies to invest or expand in France.

This mood is clearly shared by The Conference Board's panel. "The outlook for the French economy is now somewhat more subdued, as government policy is not expected to be as stimulative as thought earlier." "The government's aim is to reduce inflation to 10 percent at the end of 1982 and 8 percent for 1983. Economic growth is projected at 1.7 percent this year and 2.5 percent in 1983. No real improvement in the investment climate is expected until well into 1983."

A similar somber scenario is depicted by another panel member: "The Mitterand government will have to temper its avowed policies by economic reality in order to succeed. Initial impetus will come from consumption, but longer term growth hinges on an investment revival. Reduction of unemployment, together with the nationalizations, will prove costly. Heavy budget deficits and double-digit inflation are likely to persist." Unemployment will remain a problem, however: "The French labor force will continue to grow faster than those of the U.K. or Germany. Thus, the number of unemployed will keep rising over the next four years and the unemployment rate will still be high in 1990."

Another panel member summed up the French situation:

> "The contour of the projected recovery remains unchanged. It continues to be an example of classic Keynesian reflation in an otherwise monetarist world, with deficit spending by the government increasing consumers' incomes and encouraging their expenditures, while inflation persists and investment and trade suffer because of shrinking margins and eroding competitiveness.
>
> "We expect government spending to rise by a real 5 percent this year, with consumer expenditures increasing by nearly 3 percent after inflation. The rise in consumer spending will be made possible by a 1 percent increase in real wages, continuing transfer payments from the public sector, and a decline in the rate of saving as the economy continues to recover, reducing—at least at the margin—the fear of joblessness.
>
> "Nevertheless, the unemployment specter continues to hang over the economy despite the government's dedication to Keynesian economic programs. Shrinking markets, continued high inflation, and the mounting cost of work-sharing programs (e.g., the shorter workweek, longer vacations, etc.), all of which are supposed to be granted by industry with no compensating loss of pay, have reduced profits and eroded profitability. As a result, despite the expected recovery of demand and continued government attempts to encourage investment, private-sector expenditures on plant and equipment are still forecast to decline by a real 7 percent this year and to grow at a subpar 5 percent in 1983. At this rate, even by the end of next year, private capital spending will still be below its levels of 1980."

The economy of *Germany,* the wunderkind of the 1960's, has fallen on hard times. Terms such as "slow," "sluggish" and "doldrums" pervade the assessment of that country by The Conference Board's panel. The outlook is summarized neatly and succinctly by one panel member: "Having much more trouble than the economy 'should' have, given its basic strengths. High interest rates have been death to investment and the stubbornly strong U.S. dollar has kept inflation pressures on, leading to tighter policies. We see weakness (no growth) in mid-1983, following a strong fourth quarter in 1982 and first quarter in 1983. This keeps 1983 annual averages for GNP and industrial production down. Both government and private consumption are expected to grow more sluggishly than in the past. Germany will be focusing on reducing the public-sector deficit and making

additional investments in capital to support exports and energy conservation."

These views are echoed by another panelist: "Germany's economy remains in the doldrums despite strong overseas demand for its automobiles. With unemployment up to 1.8 million, consumer buying is still weak and construction activity remains depressed. In traditional German style, business sentiment remains gloomy about both the short-term and longer term prospects. The recession's harvest of declining profits and rising bankruptcies is only part of the reason. There is also concern about Germany's export competitiveness, Japan's inroads into Germany's markets at home and abroad, and fear that unemployment will remain high for the rest of the decade."

The overriding importance of these developments is underscored by the fact that debate over the appropriate economic policy helped widen the gulf between the two partners in the 13-year-old ruling coalition, the Social Democrats and the Free Democrats. Eventually, the already fragile consensus on economic policymaking once shared by the two parties broke in mid-September, leading to the collapse of the government of Chancellor Helmut Schmidt. While *The Wall Street Journal* ventured the guess that the new government of Christian Democrats and Free Democrats was likely "to bring more change in accent and rhetoric than substance," *The New York Times* felt that the new leadership would lead to "broad shifts in both the tone and content of Bonn's economic policy." Indeed, in the long-term strategy proposed by Dr. Lambsdorff, the Free Democrat Minister for Economic Affairs—with its emphasis on stimulating investment, creating jobs, and trimming government spending—a British observer has seen "a West German version of Thatcherism."

Several panelists, although writing during the Summer, foresaw such a change and commented accordingly. "German voters are not likely to turn—at least, not yet—to the Christian Democrats. But if the government fails to check the now-rising unemployment rate, the opposition may look more attractive to voters." "A shift of control of the government to the Christian Democratic Party need not necessarily be detrimental to the economy, but uncertainties of the ongoing power struggle add complications to the difficult task of restoring the German economy's forward momentum." "A CDU government, either alone or in partnership with the FDP, would be warmly welcomed by the business community, even though the present government is not antibusiness."

Economic conditions outside Germany were seen as determining German business activity over the short run. "Exports continue to be the mainstay of the German economy. Because the Deutsche mark's recovery is likely to be gradual, and because Germany's inflation rate is one of the lowest in the OECD, German products should remain competitive in world markets."

"Low inflation and continued gains in productivity will be positive factors and domestic manufacturers are likely to shift increasingly toward export markets to compensate for lackluster domestic sales. By the end of the decade, this trend should make Germany even more dependent upon foreign markets than it is today."

Yet, even if business activity picks up in 1983, reflecting recovery in the United States and an improvement in world trade, the growth rate projected for Germany "looks sluggish compared with previous business cycles, reflecting a subnormal world recovery and a shift toward greater restraint by both government and consumers." Indeed, even under the best of circumstances: "Over the next five years, growth is forecast to average 2.5 percent—a rate which is below that achieved from 1975 to 1980. Growth in the consumer and government sectors will be limited, while the export and investment sectors will outperform the overall economy." Meanwhile, in October the German Economics Ministry came out with a revised forecast, of zero growth, for 1983 as a whole.

Italy continues to amaze most observers. An Italian journalist noted not long ago: "The Italian economy always defies straightforward analysis, but rarely have its apparent contradictions been so marked as at present. On the one hand, there is no lack of evidence of genuine economic vitality and increased productive capacity, but matching this are just as many examples of inefficiency and even crisis." That view is echoed by a panel member: "Very mixed signals, as always, coming out of Italy. Underlying vitality continues to be crimped by government attempts to get control of deficits and inflation." Italy has even been called (by *The Economist)* "in many respects the most advanced of the developing countries (although Italians would wince at the description)."

It tends to be forgotten too often that, in the second half of the 1970's, Italy—which did not start large-scale industrialization until the 1950's—was the fastest growing of the major European economies, even though it has to import nearly all of its energy. Italy has, in fact, been catching up fast; and it is estimated that, in 1982, its per capita GNP, at around $7,300, will come close to that of the United Kingdom ($7,750). The country is expected to continue to register one of the best growth records in Europe over the next five years.

In any discussion of the Italian situation, two aspects inevitably come to the fore. The first is the alleged instability of the country's political system. Yet, Italy has been ruled by the same major party, the Christian Democrats—in coalition with a number of the smaller ones—since the end of World War II. What periodically are billed as government crises have been characterized as "the jostlings for power of ambitious brokers of patronage in these parties; they would be called cabinet reshuffles elsewhere." This is recognized by one panelist:

"Despite outward appearances, the political system is quite stable. The individuals change, but the ruling party has remained in power since the mid-1940's and, through compromises, has found workable solutions which permit the country to function."

The second issue concerns the indexation of wages, the famous *scala mobile,* under which wage earners have been compensated periodically for 70 percent of price rises. By offering virtually automatic protection against price increases every three months, the *scala* had ensured that inflation remained a built-in feature of the Italian economy. At the time of last year's survey, the Italian government had proposed replacing the system by adjustments based on a "target" set for the annual increase in the cost of living. In June, 1982, the country's employers' association, Confindustria, proposed termination of the agreement as of January 31, 1983.

Comments one panelist: "High unemployment has weakened labor's bargaining power; the timing of Confindustria's decision to revoke the *scala mobile* is, therefore, quite opportunistic. The employers' federation has, however, proposed a seven-point pact to replace the *scala mobile* which includes, among other things, partial inflation adjustments every four to six months instead of the current three months. It is possible that this proposal, in combination with the government's willingness to appease labor in other ways and labor's own weak bargaining position at present, could finally bring significant changes in wage indexation before year-end."

Another sees Italian unions as "likely to be more flexible; union ideology now concedes the need to enhance productivity." Still another writes: "There is a growing consensus among all groups—government, unions and industry management—that inflation rates must be lowered. Since the peak rate of 25 percent reached at the end of 1979, inflation rates are likely to remain around 15 percent per year, well above the levels prevailing in the economies of Italy's main trading partners."

In general, the panel believes, attitudes toward foreign investment will remain positive. "None of the major political parties, including the Communists, favor nationalization. On the contrary, the near future will bring more denationalizations. Corporate taxes will also continue to be low. Incentives will be available to attract foreign capital to the southern *mezzogiorno* region."

This section of the report, on the *United Kingdom,* was drafted on the day last September on which the British public had to do without national morning newspapers, all television channels went blank for part of the evening, buses were not running for a few hours, no coal was being dug, and civil servants were downing their pens. This "day of action," organized by the union leadership in support of the health and hospital workers' 12 percent wage claim, came just as British unemployment had hit 12.7 percent. With slightly over three million unemployed, September was thus the third consecutive month the number of jobless exceeded that registered during the depression of the 1930's.

In a way, these two developments show both the general dissatisfaction with, and the failure of, the present government's economic policies. Indeed, opinion remains quite divided over the near-term economic outlook. Despite the government's brave assurances that recovery is under way, the business community has remained decidedly gloomy. Thus, the Midland Bank noted recently that "the seeds of recovery in the U.K. economy which seemed to be germinating in the autumn [of 1981] have subsequently shown few signs of growth," and that the general picture was that of an economy "which seems to be doing little better than bump along the bottom."

The Conference Board's panel seemed to be leaning toward a stance of cautious optimism, although it saw the British economic position as "far from satisfactory." Here is a sprinkling of views:

- "Some sort of trough has probably been reached, but it is hard to be too optimistic. The United Kingdom has stayed down for so long, but still convincing evidence of any upsurge is missing."
- "Economic recovery has been weak and hesitant in the United Kingdom but it remains, nonetheless, on track."
- "After two years of precipitous decline, the economy reached its trough in mid-1981 and now seems to be at the start of a mild upturn. Modest real GNP growth averaging 2 percent per year is expected over the next five years."

Any such upturn, it is generally agreed, hinges on more expansionary measures that, in turn, may well be dictated by the political timetable. "As the next general election has to be held before May, 1984, the easing of Prime Minister Thatcher's tight-fisted economic policies seems probable next year. Even a group of her own Tory members of Parliament are advocating the introduction of stimulative measures this Fall."

"With the next general election only two years away, the Thatcher government will grow increasingly aware of the need to secure victory through a reflationary package early in 1983."

Such a package—which would constitute "acknowledgment of reality"—would have some interesting implications. "In 1983-1984, inflation is expected to rise again as economic policies become more stimulative. The next government, in the event of escalating prices, is likely to impose some sort of wage-control to reduce the inflation rate toward the target level of 7 to 8 percent. Growth will reach a cyclical peak of

about 2.5 percent in 1983-1984, but wage-control policies will restrict the economy to low positive growth rates thereafter."

In light of these developments, a sustained strengthening of sterling is seen as unlikely, "given the decline in oil prices, poor comparative real interest rates, and concerns that an electoral defeat of the Thatcher government would reopen the door to exchange controls." However, "import controls and exit from the European Community are unlikely unless Labour wins an absolute majority."

Meanwhile, at the end of October, *The Economist's* weekly barometer was pointing to "change" and the overall outlook continued mixed (see box).

Barometer

Pay is now being squeezed, along with prices. Average earnings in August were 7.8% up on a year earlier, the smallest annual rise for five years. That has not stopped retail sales from rising briskly—in real terms by 2½% in the July-September quarter, up 3% on the same period in 1981.

Companies also boosted their spending, by 4% in nominal terms in the second quarter, thanks to more investment and less destocking. But their income fell, pushing them into a large (£1.3 billion) deficit for the first half of this year, after a £1.8 billion surplus in 1981. The index of leading economic indicators rose 2.3% in September.

Source: *The Economist*, October 23, 1982.

Other Countries

This section presents selected comments by panelists on eight additional countries.

"Argentina's main economic problems in the next five years stem from the extremely depressed economic conditions existing before the Falklands conflict. To these, one must now add higher inflation, a weaker balance of payments, and the possible need to restructure the foreign debt. Stiffer restrictions on foreign investment over the five-year period are likely."

"Against the background of hardly any growth in the OECD countries this year, it is difficult to see any upturn ahead for the *Australian* economy, particularly in view of the divergent trend in inflation between Australia and its major trading partners. Due to excessive wage demands, high interest rates, increased public-service charges, and higher domestic oil prices, Australia's accelerating consumer price index is out of line with the disinflationary trend in most industralized countries."

"The longer term outlook for *Brazil* hinges heavily on the government's ability to keep the balance of payments in order, and yet manage a delicate growth and inflation situation. The country has succeeded before in directing the economy to the area it wanted. There is good reason to believe it will again."

"Most of *Brazilian* capital is going toward servicing the public debt. There simply is not any capital available for development projects—except those projects that will generate badly needed export earnings. The size of Brazil's public debt will be a drain on the Brazilian economy through the 1980's and likely into the 1990's."

"Hong Kong is expected to maintain high economic growth in the coming five years. What Hong Kong lacks in natural resources, it makes up for in export competitiveness. Its skilled and efficient labor force, increasing economic ties with China, and good infrastructural facilities confirm that Hong Kong's high growth momentum will continue."

"Hong Kong is slow. The lease question with China is greatly slowing construction. Cost and space problems are cutting down on manufacturing. The bloom is off the rose. People are moving to China and investments to Singapore."

"Korea is in a stage of transforming from a light-industry to a heavy-industry oriented economy. Fundamental problems like the lack of technology and management skills, streamlining the overinvested petrochemical industry, and the inability to successfully develop indigenous and complementary industries are hurdles that will check Korea's economic growth over the medium term. Restrictive policies and low wage increases have indeed helped to bring inflation under control. There is wide consensus that the rate of price increases will be kept down, based in part on the Korean government's strong determination and the variety of anti-inflationary measures available."

"Mexico finds itself in a period of consolidation with growth rates for this year and next projected to be only in the 3 to 3½ percent range. In contrast, inflation is forecast to run in the 45 to 50 percent range, an aftermath of the recent devaluation and mandated wage increases for lower income workers."

"Without a strengthening oil outlook by 1985, the possibility does exist for *Mexico* to be plunged into a prolonged period of little or no growth. The political consequences would be extremely serious: widespread social unrest and a possible hardline response from the government toward business and labor."

"The outlook for *South Africa's* economy and for the economic policies of its government hinges largely upon future trends in the price of gold. We look for several more months of intermittently downward pressure on the precious metal, with adverse effects on production, the

external accounts, and the currency, resulting in additional government efforts to check demand and inflation. Moreover, we expect a generally lackluster price performance for gold even in 1983 as world inflation remains within bounds. However, the metal's price is likely to begin rising by mid-1983, as the world economy moves into a more robust recovery phase."

"The *Taiwanese* government is projecting a growth rate of 8 percent in 1982-1985. The achievement of these targets depends on: first, the world's economic health; second, Taiwan's ability to shift away from labor-intensive sectors to technology-intensive industries; and, third, its ability to change its domestic cost structure to withstand stiff competition from Korea and lower wage countries in Southeast Asia. In the short run, we believe that the 8 percent target for 1983 is overly optimistic, even though the projection is conservative compared with the historical 9 percent average annual growth in 1952-1980. Generally poor economic conditions will dampen hopes for any high export-led growth. Investment may increase somewhat and add to economic growth as a result of the government incentive program. Over the medium term, Taiwan may continue to grow at respectable rates of around 7 percent as a result of improvement in technology. Trade will probably be the chief engine for growth, assuming that Taiwan is politically capable of gaining access to foreign markets."

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Labor Outlook, 1983

by Audrey Freedman et al

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THE CONFERENCE BOARD'S 1983 LABOR OUTLOOK PANEL

DONALD Y. CLEM
Chairman of the Board
and Chief Executive Officer
McConway & Torley Corporation
Pittsburgh, Pennsylvania

DONALD EPHLIN
Vice President
United Automobile, Aerospace and
Agricultural Implement Workers
(AFL-CIO)

DAVID LEWIN
Professor of Business
Graduate School of Business
Columbia University
New York, New York

DANIEL J. B. MITCHELL
Director, Institute of Industrial
Relations
University of California
Los Angeles, California

ROBERT NEYLAN
Vice President
Employee Relations
Gould Inc.
Rolling Meadows, Illinois

PETER J. PESTILLO
Vice President—Labor Relations
Ford Motor Company
Dearborn, Michigan

WILLIAM W. WINPISINGER
International President
International Association of
Machinists and Aerospace Workers
(AFL-CIO)

AUDREY FREEDMAN
The Conference Board

Chairman

The Conference Board's annual session on the labor outlook took place on November 4, 1982. Panel members discussed the current economic situation, compensation trends, labor relations, and political events. This process provided the predictions for 1983. The individual views quoted were submitted in writing.

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THE CONFERENCE BOARD, INC.
845 Third Avenue, New York, N.Y. 10022
THE CONFERENCE BOARD OF CANADA
25 McArthur Road, Ottawa, Ontario, K1L-6R3, Canada
THE CONFERENCE BOARD, INC.
Avenue Louise, 207 Bte 5, B-1050 Brussels, Belgium

AUDREY FREEDMAN
The Conference Board

Chairman

LABOR OUTLOOK, 1983

Recession's Effects in 1983

The Conference Board's Labor Outlook panel expects unemployment to remain high—close to current levels—throughout 1983 (see Table 1). As a consequence of the recession and falling prices, it foresees some further reduction in wage increases. In 1983, the panel thinks that consumer price inflation will increase somewhat, to about 6 percent. There will be little payroll growth in any 1983 business recovery, according to the panel, which was concerned that the 11½ million currently unemployed may never be fully reabsorbed into the work force. Consequently, the panel members raised proposals for public works programs (financed by reduction in defense spending, if need be), and government-backed industrial development bonds to raise capital for small business. There was also discussion of national economic planning, as opposed to industrial and employment "programs." (See page 9.)

During 1983, any recovery in production levels, accomplished by a much-thinned work force, will yield solid gains in output per worker hour. Following this line of reasoning, the panel concludes that unit labor cost increases in manufacturing will average 3.5 percent next year—about half the current rate of increase.

Table 1: Forecasts for 1983 by The Conference Board's Labor Outlook Panel

	Median (Percent)	*Range (Percentages)*
Unemployment average during 1983	9.7	8.9 to 10.8
First quarter	9.9	9.7 to 10.8
Second quarter	9.8	9.2 to 11
Third quarter	9.7	8.5 to 10.7
Fourth quarter	9.4	8.2 to 10.7
Rate of inflation (average increase in Consumer Price Index)	6	5 to 7
First-year wage and benefit increases in major union contracts	6.9	6 to 7.5
Overall increase in average hourly earnings, January, 1983 thru December, 1983	6	3.5 to 9
Increase in labor costs per unit of output in manufacturing	3.5	2 to 5

Price and Wage Inflation Sharply Down

Falling sales throughout 1982 have cut price inflation in half. Wage inflation has fallen even further. In the first three quarters of 1981, first-year increases in major collective bargaining settlements averaged 11.5 percent. This abated to 3.8 percent by Fall, 1982. Some two-fifths of the workers covered by new 1982 bargains received no wage increase, greatly lowering the weighted average. When their "zero" bargains are removed, the average first-year increase in bargains concluded from January through September, 1982, is 7.1 percent (note the similar rate of wage increase in Chart 1). State and local government employees bargained average increases of 8.1 percent.

DAVID LEWIN
Professor of Business
Graduate School of Business
Columbia University
New York, New York

David Lewin suggested that industry experience varies, even within a very serious recession:

> "This is a case in which the disaggregated data tell a clear story. Unionized workers who received small or no (zero) wage increases in 1982 were employed in firms and industries that faced depression-type, if not bankruptcy-threatening, conditions. The economic survival of many of these firms and industries was (and remains) in question and fundamentally affected wage bargains in 1982. The transportation, automotive, rubber and farm equipment firms are the best known of these facing crisis conditions; but many smaller, lesser known, often supplier firms are experiencing the same circumstances. In contrast, a

minority of firms and industries did not face crisis conditions in 1982. Indeed, some firms experienced rapid growth and high profitability—and their unionized workers received more 'normal' rates of pay increase. From this experience it can be seen that collective- bargaining settlements provide another example of the 'fallacy of averages.'"

ROBERT NEYLAN
Vice President
Employee Relations
Gould Inc.
Rolling Meadows, Illinois

The wage leaders of the 1970's are, in many cases, the same parties who now are negotiating cost-of-living (COLA) clause "suspensions," wage freezes, reductions in paid time not worked. Robert Neylan said:

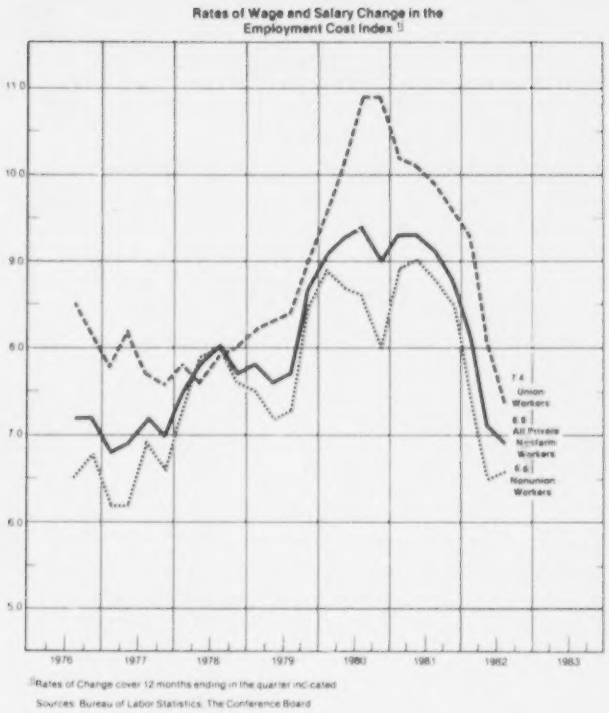
"This interesting development is a function of recession, but also has implications for the future. I suggest that the 'pattern' practice, which so much dominated bargaining during the 1960's and into the 1970's, has suffered yet another blow. Employers and unions, too, are increasingly conscious of the impact of a settlement on 'their' jobs, rather than concentrating on keeping up with the Jones. The auto pattern is dead for the moment at least, although in the media Chrysler workers still refer to the fact that GM employees are ahead. Profit sharing and job guarantees are becoming more common, if not yet commonplace, and the health of individual businesses is becoming the focus of bargaining. If we postulate a slow recovery from recession, these trends will become more pronounced, although the notion of 'follow the leader' in heavy industry will die hard. Increase patterns escalated by price inflation, rather than the employer's balance sheet, will be tested as more employers (and employees as well) recognize that the time has come to bury cost-of-living clauses."

Some insight on the auto bargain—and its leadership role—was provided by Peter Pestillo:

"We sought and achieved labor-cost moderation in the latest agreement. The Japanese manufacturers have a labor-cost advantage derived from compensation costs half ours. We will narrow—though not close—this gap during the life of this agreement.

"I think it is to the great credit of our senior management that no one ever suggested the quick fix of deep wage cuts. The company has been around for almost 80 years

Chart 1



[1]Rates of Change cover 12 months ending in the quarter indicated
Sources: Bureau of Labor Statistics, The Conference Board

now, and we have chosen a course that might be less flashy but more fulfilling. We have chosen to begin a process *leading to* a cure of our noncompetitiveness, not just to provide some quick, and perhaps temporary, relief from it. We bet that deep wage cuts would not survive adversity.

"There will be no general wage increases under this agreement, and paid time off was dramatically reduced. COLA payments were suspended for 18 months, though they must be revived (but not repaid) before the agreement expires. We introduced profit sharing as a means of giving our employees a direct stake in our recovery. We hope over time to extend this move toward profit sharing and away from COLA as a means of permitting the company to retain money when it is needed more. But, as I said, we did not feel we could fix everything at once.

"We provided job or wage guarantees to senior workers

PETER J. PESTILLO
Vice President—Labor Relations
Ford Motor Company
Dearborn, Michigan

and agreed to experiment with lifetime employment. In doing so, we knowingly made labor cost less variable. We changed the employment equation toward the Japanese—or European—mode, a system with which we are fully familiar. We did so out of a conscious intention to make a commitment to our people that we expect to be reciprocated. There are cost safeguards on this job security; and if we can manage our business well, this need not be an expensive benefit. We have made significant progress locally in achieving work-rule modifications."

DONALD EPHLIN
Vice President
United Automobile, Aerospace and Agricultural Implement Workers (AFL-CIO)

Don Ephlin, the union officer who negotiated that agreement with Ford, made it clear that wage cuts will not become a pattern:

> "We have proceeded strictly on a case-by-case basis, all too aware that the times are ripe for many companies simply to want to climb on the 'relief bandwagon.' At the same time, we look for 'quid pro quos': lifetime-income guarantees, profit-sharing plans, financial disclosure, and 'equality of sacrifice' clauses among management personnel."

Dan Mitchell's description of the occasions on which concessions are useful suggests that union resistance (up to the point of actual payroll reductions) is rational:

> "Certain industries and employers are in dire straits and can credibly ask unions for wage concessions to conserve jobs. When the job security of senior union members is threatened by plant closings, mass layoffs, or bankruptcy, the union political mechanism is obviously going to be more receptive to some type of concession.
>
> "However, while many employers appear to have asked for concessions during the past year, not all could document that jobs could be saved. For firms that are not in severe economic distress, even a substantial decrease in wages will have only a modest effect on costs and prices. A firm in which labor accounts directly for about 20 to 25 percent of total costs—and which receives a wage cut of 10 percent—could reduce prices by only 2 to 2.5 percent as a result. Such a modest reduction would probably not result in much added demand for the firm's product. Thus, the wage cut would not have much effect on employment or job security.

DANIEL J. B. MITCHELL
Director, Institute of Industrial Relations
University of California
Los Angeles, California

> "Wage concessions have a job-saving effect *only* when the firm or plant is near the shutdown point. Under those circumstances, even a modest saving in labor cost can be the difference between operating or not operating."

Even with the variation among major manufacturing industries, a reduction in wage inflation is clearly taking place. Among service industries, however, the extent of response to recession is less obvious. Dan Mitchell suggests that there is general reduction in the rate of wage increase here, as well:

> "There are no sectors whose wage decisions are permanently immune from the forces that have slowed the average rate of wage increase. Price inflation is a major determinant of wage inflation. Since price inflation has slowed, wages throughout the economy will eventually react.
>
> "The service sector has not been the scene of major wage-concession negotiations because (1) many parts of that sector are heavily nonunion, and (2) the sector is less sensitive to business-cycle pressures. From August, 1981, to August, 1982, the hourly earnings index for 'services' rose 7.5 percent. But from August, 1980, to August, 1981, the figure was 10 percent.
>
> "Nonunion employers in that sector are being less generous with discretionary pay adjustments under merit plans. Actual pay increases can be slowed by employers through a tightening of internal policies with regard to pay adjustments that do not show up in official pay schedules."

Some service industries are growing even during recession, and some are not facing competitors with lower costs of production, observed Don Ephlin:

> "The severity of the recession's impact has been decidedly milder in services than in other industries, but not all workers in the industry have been spared. In education, for example, there have been drastic cuts at all levels, the product of declining enrollments and shortage of funds.
>
> "The largest industries within services—health-care services and business services—have kept on adding to their payrolls throughout the recession. Driven by high interest rates and overstocking, many businesses have continued

the computerization of their accounting and inventory systems to cut down on financial costs.

"One of the reasons for higher wage increases is the virtual insulation of most service industries—at least so far—from foreign competition."

DONALD Y. CLEM
Chairman of the Board
and Chief Executive Officer
McConway & Torley Corporation
Pittsburgh, Pennsylvania

In agreement, Donald Clem said:

"Service industries are still growing and are not really in a recession as compared with the manufacturing sector of our economy and, therefore, there has not been the need to respond with reduced wage improvements. There are some competitive forces at work, but I do not expect that there will be a sharp plunge in wage increases in the service industries as has occurred in almost all other industries.

"Hotels and other personal services ultimately will feel the impact of the recession through the tighter controls on corporate-expensed dollars. For example, our sales and executive personnel now use their automobiles on trips of less than 500 miles, and usually stay at a motel outside of the major city rather than in an expensive downtown hotel.

"Advertising should be a growth industry in periods of recession, since there is a stepped-up sales effort during these depressed times. However, that is an easy dollar to cut and, I suspect, they reduce advertising expenditures in the smaller corporations even though they should be doing the opposite.

"There will certainly be more strikes in the public education system. Local communities are up in arms over the continued pressures to increase local taxes—either income or property—to pay for inflationary settlements. I believe it will be difficult for the union teachers to continue to get contract settlements above the inflation level once we have stabilized lower inflation over an extended period of time."

1982 Affects 1983

Wage increases in 1983, the panel agreed, will remain at their 1982 levels. In major union negotiations, the average increase is expected to be just under 7 percent. There was close agreement among panel members on this point: Their estimates ranged only from 6 to 7.5 percent. (See Table 1.)

Using a broader indicator of wage change—average hourly earnings gains—the panel predicted an increase of 6 percent during 1983. There was more divergence among panel members on this point, however. This suggests that some feel that the nonunion work force will continue to be affected by recession and a labor market full of job seekers in every occupation and area. Only one panel member expects wage increases to resume their pre- recession growth.

The year-long question of 1982: "What will be done about steel wages?" will be answered in the next few months. Pressure on the parties to break the automatic wage pattern has never been greater, but negotiating failures have so far prevented an early opening of the major steel contract. Before it terminates in Summer, 1983, a change in wage terms seems likely. However, the panel was not completely confident that a strike is out of the question. Mr. Neylan suggested that several conditions are now present that parallel those of 1959—just before the last big steel strike:

"It is interesting to compare the response of two industries, steel and auto, to essentially the same problems. How does it happen that the auto workers' leadership can sell its militant membership on the notion of accommodation while the steel workers' leadership, taking a moderate tack, fails? I believe that the answer is to be found in the history of steel bargaining and in the response of management to industry problems. *The leadership of the steel union has followed management's lead in ignoring problems that have been growing for years, problems related to pricing, quality and product mix.* The easiest course for management was to pour out unsophisticated product during the 1960's to cash in on the construction boom. Wages, salaries, benefits and dividends were raised as if there were no tomorrow. Foreign competition was condemned as 'dumping' by both sides in an effort to preserve the status quo. The nine-year no-strike agreement was a response calculated to dampen foreign competition, but it also served to limit the bargaining to immediate problems and buried the long-range realities.

"*The one reality that the industry has never addressed is the loss of its monopoly in the American market.* True, dumping does occur, but the more efficient foreign producers do not have to dump to undercut U.S. companies in this marketplace. The steelworkers as individuals, I am sure, recognize what is happening today. The industry is playing hardball in an effort to achieve concessions that will reduce cost, shore up its financial condition, and provide capital for investment and modernization. The other side of the coin, some form of guarantee that jobs will not disappear anyway, does not appear to be part of the industry program—and that is what the workers want. Any employee of U.S. Steel has to be painfully conscious of the fact that the company has reinsured part of its wager by investing in oil. While Chrysler divested itself of peripheral operations (air conditioning, tanks, leasing), admittedly under different circumstances, 'big' steel is scrambling to put distance between itself and its roots.

"We may be looking at 1959 all over again. Recall that in 1958-1959 the industry was operating at capacity levels

On "Concessions"

"The untold story, unreflected in any statistics, are the concessions being squeezed out by companies through premature reopening of negotiations. In many industries, management has caught 'concession fever'. And that includes just about every company that deals with a union—even the profitable ones. In industries where layoffs have occurred, the workers are naturally responsive to company claims that wage concessions must be given if the company is to compete effectively. If this does not work, the threat of plant closure often does. We have tried to limit these take-aways by instructing our locals to demand specific proofs before talking about concessions.

William Winpisinger

comparable to the present. The companies gambled, with a high stockpile of finished goods, that they could recoup some of the concessions (principally work rules) given away over the years. If the industry miscalculates again, the confrontation will be equally devastating and may well answer the question whether we are to have a viable domestic steel industry."

Returning to his thought that only under the real threat of plant shutdown are concessions readily (and justifiably) granted, Daniel Mitchell said:

"Steel bargaining is highly centralized, with multiemployer bargaining in basic steel since the 1950's. Thus it may be difficult for workers in local, marginal plants to have a substantial influence on national policy. For example, concessions negotiated locally at the Kaiser Steel plant in the Los Angeles area were vetoed by the national union. It can always be argued that local concessions would trigger across-the-board concessions, affecting plants not facing imminent shutdown.

"With regard to the failure to open the current contract this past Summer, the parties focused too heavily on the August 1 deadline. While it is sometimes useful to have deadlines, the fact that a pay increase would be effective on that date was not sufficient rationale for a deadline. It is evident that management is looking for a long-term change in wage trends in the steel industry. Such an understanding, if it can be reached at all, would require that management put forward a credible long-term argument to the Steelworkers with convincing evidence for the effects on job security. In turn, the union would need considerable time to sell such a proposition to its membership."

Donald Clem describes some of the negotiating problems faced by management:

"This will be the first contract negotiated in many years that is not under the 'no strike' agreement. The 'no strike' agreement was probably the worst thing that ever happened in labor negotiations in the steel industry. The guarantee of a quarterly cost-of-living increase and a minimum of an additional 3 percent annually prevented the steel companies from making adjustments in their labor rates over almost a decade.

"Now there is a mass effort on the part of the steel companies to admit their errors in labor settlements of the past and to try to get the worker to identify with the competitive situation. This is very difficult for the steel companies to accomplish, mainly because the worker will ask: 'If we make concessions, what guarantee do we have of job security in the world market for steel? How many new jobs will be added if we make concessions?' The answer to this might just have to be: 'No more guarantees than you have had in the past—there are probably going to be fewer jobs in the immediate future.'

"In our experience, it has been very difficult to get the worker to relate to domestic competition, let alone foreign competition. The U.S. steelworker cannot grasp the importance of productivity and the labor rate in maintaining job security.

"We have had a unique experience. We purchased another foundry and modernized it to become the most advanced steel company producing our product in the country. We also obtained a superior work force, with a different union and a different contract period. The two plants can both produce the same product. Each looks upon the other as a competitor. During the current recession it was not too difficult to get concessions at the higher cost shop, and to obtain substantial productivity improvements at both plants. In addition, at the lower cost plant, we recently were able to achieve a 3½-year contract at an annual increase of less than 5 percent in wages and fringes. If the steel companies can somehow bring this competitive awareness to the majority of the employees, they should reach a settlement without a prolonged strike."

David Lewin expects some strike activity—but perhaps not an industrywide strike. Perhaps the term "industrywide," applied to bargaining, patterning or any other union-management arrangement, will never apply to steel again:

"Even if steel negotiations commence and continue up to the expiration of major contracts in mid-1983, a consensus about concessions, givebacks or modest settlements seems unlikely to be reached easily. In fact, formal strikes or wildcat strikes are likely to take place in steel before new settlements are reached. What this may also suggest is further dilution of multiemployer bargaining in steel and increased emphasis on wage individuation. Thus, bargaining in steel may soon come full circle from the nature and structure of bargaining that developed in this industry following the prolonged steel strike in 1959."

Price Inflation in 1983

The Conference Board's Labor Outlook panel expects consumer price inflation to be about 6 percent next year,

slightly higher than it was running in the third quarter of 1982. There was agreement in the group, with a narrow range of estimates from 5 to 7 percent (see Table 1). Don Ephlin attributed the quiescence of inflation to excess capacity throughout the economy:

> "Along with record unemployment rates and bankruptcy rates matching those of the Great Depression, the 1981-1982 recession has accomplished a decline in the rate of inflation. However, I must repeat that high unemployment and recession represent a scatter-gun approach to an inflation problem that is, to a substantial extent, of a sectoral nature. In other words, recession is not a *durable* medicine for inflation—unless we are willing to settle for very slow growth for an indefinite period.
>
> "In the short term there need not be immediate resurgence of inflation as the economy turns up, because many sectors in the economy, autos among them, are poised for robust increases in productivity. Obviously, management decisions vis-a-vis profit margins will be very important to the inflation outlook."

Robert Neylan and Daniel Mitchell are in agreement that inflation will remain low for several years. Mitchell explains:

> "In 1980, the underlying rate of inflation was about 10 percent. By the middle of 1982, the underlying rate was about 6 percent. This drop in the underlying rate was achieved by a period of economic slack that began in 1979, and eventually resulted in record unemployment rates. It took a heap of recession, in short, to cut the rate of inflation by 4 percent in a period of over two years.
>
> "The inertia of inflation has been long noted by empirically oriented economists. But inertia can be beneficial under some circumstances: Once inflation is dampened, it will reignite only slowly.
>
> "Given inflation inertia, there is room for a recovery to get under way without a rapid rise in prices and wages. Recovery might proceed for some time without producing strong price acceleration, although eventually, continued expansion will produce increased inflation.
>
> "The record on inflation forecasting has not been especially good, and the economy is currently operating in a range outside the usual run of observations with regard to unemployment. The UCLA Business Forecast predicts an inflation trough of about 5 percent in 1983, with some acceleration thereafter. Wage inflation is projected to reach a trough of a little over 6 percent in 1983, with accelerating tendencies thereafter. Other forecasts suggest that both wage and price inflation might be somewhat higher. If one takes long-term government bond yields as containing an inflation-expectation component, at this writing the market is projecting an eventual inflation rate in the 8 percent range."

Unit labor costs—a sharply rising element in the inflationary decade of the 1970's—will increase only slightly during 1983. The panel expects a combination of slowly rising wages and a substantial increase in productivity to raise manufacturing unit labor costs only 3.5 percent next year. Every estimate here (ranging from 2 to 5 percent) was below the current rate of increase of 7.2 percent (see Table 1). This auspicious shift—wages down, productivity up—is the chief optimistic forecast that the panel made.

Unemployment Will Remain Seriously High

More discussion was devoted to unemployment than to any other subject. The panel members are not confident that recovery will reduce current high levels of unemployment to acceptable rates. A major subject of discussion was the form that government action might take—not the wisdom or need for intervention. Daniel Mitchell said: "A robust economic recovery would bring down the unemployment rate. The notion that the rate is permanently stuck at its current high levels due to structural changes is simply not correct." Nevertheless, the time devoted to considering how an active government policy might be designed suggested that none of the panel members see that reduction occurring.

The panel predicts an overall unemployment rate of 9.7 percent for 1983, with a slight downward trend throughout the year (see Table 1). One day after the meeting, the unemployment rate reached 10.4 percent. As can be seen from the range of their estimates, some expect no improvement throughout the four quarters of 1983.

One panel member, Robert Neylan, appeared to be relatively sanguine about employment recovery:

> "In considering what becomes of the unemployed, it is worth reviewing the unemployment situation from a broad perspective. First we went into the recession with unemployment at about 7 percent to 7.5 percent, depending on the date you pick. Unemployment has been steadily rising over the past 20 years: It averaged 5.1 percent in the period 1955-1960 and 7.1 percent in the years between 1975 and 1980. The recession-induced increase in unemployment amounts to about 2.9 percent, matching the increase attributable to every prior recession since World War II. I am not minimizing the seriousness of the unemployment picture, but I do suggest that in a real sense we are no worse off than we have been in past recessions.
>
> "We were unfortunate enough to have started into recession at higher unemployment levels than we have had to deal with previously. I suggest that a gradual improvement in the economy will reduce the unemployment rate—over time—to the 'full employment' level. Included in the final number will be many permanently displaced from smokestack industries. Those with transferrable skills, or who are young enough to acquire a new skill, possibly in one of the service industries, will be reemployed, although probably at lesser pay levels than they previously enjoyed. Some will be employed only at the margin, the same thing that happened to those who lost employment when in-

dustry left the Northeast. We are not, however, talking 11 million but—rather, small consolation—perhaps one- half million."

Yet Mr. Neylan was ready to suggest that "a highway program would contribute to our national well-being while remedying a serious national problem."

Both the Machinists and the Auto Workers unions have been advocating for several years an "active" government policy to promote employment. In previous years, panel members gave only brief attention to the matter. This meeting devoted a substantial part of its time to discussing what the government might do. Mr. Neylan's proposed restoration of highways and bridges, for example, was accepted by the group and a source of funds suggested: redirect defense expenditures. Commenting on this, one panel member said: "The unemployment situation is such a serious social threat to stability that we could appropriately call a highway program a genuine 'defense' expenditure." The group also generally agreed that "recovery will not come naturally without such a program to help reduce unemployment."

Another proposal, raised at the panel meeting, would have state governments issue industrial development bonds with the proceeds to be used by small private industry. A council of small industry at the local level would allocate, and help management of small businesses use, this capital.

The group saw three purposes in its various proposals:

- to lower unemployment
- to "pump money into the economy"
- to invest in basic facilities

The term "economic planning" came up and was not rejected out of hand. However, one member observed that with each recent recession, peak unemployment has been higher—yet there has been no massive turning out of politicians. There is no consensus "yet," he observed, for economic planning. The 1982 election did not focus on the issue.

The Election and Choices for the Future

A discussion of the effects of the 1982 election on Administration policy produced little agreement. One member suggested that defense spending will be redirected toward more labor-intensive activities in mid-1983, and the whole government will engage in "active, artificial" stimulation as the Presidential election year of 1984 begins. Another member pointed out that the Federal Reserve had "loosened up" on the money supply prior to the election. He predicted that the Federal Reserve would become even more liberal this winter and next spring.

Defense expenditures had been mentioned several times when one panel member met the subject head on. He observed that the electorate had "not seriously faced the main issue yet: how much defense do we want to buy—and what is the real price?" He thinks the answer might be "much less" because of the trade-off in reduced investment in our domestic "capital equipment" (roads, bridges, transportation systems, housing, education, etc.) and in social stability. Mr. Reagan, he said, has not clarified what his military goals are, yet "we are accelerating weapons hardware to the point where we are tempted to use it." He also noted: "We are buying sophisticated and fragile weapons that we are not even able to maintain in usable condition."

WILLIAM W. WINPISINGER
International President
International Association of
Machinists and
Aerospace Workers
(AFL-CIO)

Mr. Winpisinger advocated a comprehensive national recovery program that would include Mr. Neylan's highway restoration as an element:

> "We have advanced a number of proposals designed to meet critical unmet needs that have been neglected too long. This includes the badly deteriorating national infrastructure.
>
> "The IAM has designed and is advocating a program for rebuilding America. Rather than rely on the private investment decisions of a few giant multinational corporations, which represent a new sovereignty in the world, the IAM approach calls for national economic investment and production coordination, much as was used during World War II, with special targeted assistance to small-and medium-sized businesses that are now pretty well shut out of international trade. This is an adaptation of the kind of national economic planning long practiced by the United States' major trading partners in the NATO countries as well as Japan and Sweden. Most of these countries have stronger trade unions, higher wage levels, better access to health services, less unemployment, and lower inflation than the United States.
>
> "Other parts of the IAM package call for restructuring the energy industry and establishing a national health service. All parts of the program would require considerable trade-union and local-community involvement in planning and decision-making processes, particularly with respect to industrial plant shutdowns and plant relocations."

Some proposals were in favor of reinstitution of the human-resource investment programs of the early 1960's. Mr. Neylan said:

> "The Manpower Development and Training Act of 1963 was directed at upgrading skills in depressed areas and may have played a part in the development of the Sun Belt. Southern states, like North Carolina, have carried on similar programs, integrating industry into the process with considerable success."

Professor Lewin suggested another direct investment in reducing structural unemployment—a labor mobility program:

> "I would like to see a program of relocation allowances to encourage the movement of excess labor supplies to areas of excess demand. Even now, unemployment is not evenly distributed among economic sectors or occupations, structural unemployment apparently is on the rise, and unemployment responds more slowly than prices or wages to economic expansion. Encouraging labor mobility can, therefore, produce some reduction in unemployment.
>
> "Such relocations often involve the upheaval of personal, social, family, religious and other relationships. A program of support to ease these burdens seems to me to be both prudent and efficient. I also believe that selected extensions of unemployment insurance could and should be undertaken, for example, in specific geographical areas or occupational groups that have experienced particularly severe unemployment."

Donald Clem described an experience that suggests immobility among the unemployed—and that unemployment insurance is not arranged to create incentive for change:

> "What will happen to the 11 million currently unemployed? They will ultimately be absorbed by the balance of the economy but with some major problems. Union workers, unfortunately, are not very mobile. There will be little or no attempt on their part—based on past experience—to seek jobs (especially lower paying ones) until their current unemployment benefits expire. In recent years, when we were expanding in Pittsburgh and a neighboring forging plant, which at one time had employed over 1,000 people, was closing its doors, we were unable to attract even a single person, particularly in the skilled areas of maintenance, machining, crane operation, and so on. Why? Because they not only received Unemployment Compensation, but additional moneys, since they were supposedly put out of business by foreign competition. Unfortunately, when their benefits ran out, we were not hiring."

Linking payments to willingness to relocate, and to performance in a training program (as has been proposed by the Administration) might be one way to overcome the conservatism noted by Mr. Clem.

Don Ephlin reminded the group that:

> "Both the United Auto Workers and the AFL-CIO have proposed public works, public-service employment programs, and extended UC benefits. To avoid increasing an already hefty deficit, funds for those programs could come from cuts in defense spending and from closing tax loopholes.
>
> "The continuation of the current laissez-faire policies virtually guarantees chronically high unemployment levels. That is why I believe that the laissez-faire ideologues will be dethroned, and that our society will turn toward activist government policies to maximize the number of jobs and assure a fairer distribution of income.
>
> "Although the current recession qualifies as the worst since the Great Depression, the proportion of the unemployed collecting unemployment benefits is under 41 percent—compared to 64 percent at the trough of the 1974-1975 slump. There is a need to extend unemployment insurance to protect the long-term jobless. It is disgraceful that in the state of Michigan, which has been saddled with the highest unemployment rate in the nation for over 34 months, the 13-week unemployment insurance extension is expected to trigger "off" in a few weeks.[1] At that point, only the 10 additional weeks recently enacted will be available to those who have exhausted their 26 weeks of benefits.
>
> "Training programs, and especially the new program for dislocated workers, are a step in the right direction—but they are not enough. Public-employment opportunities must be provided for the long-term unemployed who cannot find jobs. Public works are necessary if the recession is to be followed by a sustained expansion and healthy productivity growth. As has been widely acknowledged, the crumbling infrastructure is one of the reasons productivity is lagging badly. The unconscionably high number of unemployed and discouraged workers implies that public-employment programs will be necessary as well. This is an opportunity to initiate an antirecessionary public- investment program that would put many of the unemployed to work rebuilding bridges, sewer systems, railroad beds, highways and so forth."

Capital Spending in 1983

At least until late 1983, the group sees no capital spending growth. Capital budgets are still being cut, and consumer confidence is so low that there is no gleam in the eye of producers. By late in the year, Professor Lewin suggested, Federal Reserve stimulation—added to fiscal stimulation—may foster some growth:

> "I expect to see greater investment in new plant and equipment in late 1983. The reasons include (1) the economic recovery that will take place by then; (2) con-

[1]This process stops the 13-week extension of unemployment benefits. For details, see A. Freedman, *Security Bargains Reconsidered*. Conference Board Report No. 736. 1978, pp. 10-11.

tinued decline in interest rates in 1982 and stabilization, or only modest increases, in 1983; (3) growing recognition of the inferior position of U.S. industries in terms of ability to compete with foreign producers; (4) infusion of funds to certain firms and industries because of major increases in defense spending; and (5) a slight shift in emphasis from short-term to longer term investment strategies on the part of investors and, especially, managers and officials of private companies.

"The conventional wisdom about the savings- investment relationship for the economy as a whole has not proved out in recent years and new thinking is badly needed in this area. Ironically, one might have expected to see an upsurge in capital investment in 1982 when a Republican Administration, supposedly committed to supply-side economics, held sway. Since this did not occur, one should be wary about prognosticating future capital investment trends. Still, I expect to see a modesr growth of such investments in the coming year."

Robert Neylan is pessimistic:

"It does not appear that capital spending will increase any time soon, not until late 1983 at the earliest. Reduced profits, high interest rates, and underutilized capacity are the reasons. The basic outlook is for a weak recovery, unlike the 'normal' recoveries of the past. We are accustomed to inventory rebuilding, growth in housing and durable goods, and recovery is off and running. This time we are burdened with high unemployment, gross lack of liquidity in business, low utilization of capacity, high (though declining) interest rates, and worldwide recession, with an overvalued dollar having an impact on exports.

"Defense has constantly been expanding even during the recession, with order rates increasing by 50 percent more than in 1981. But defense does not have the ripple effect that autos or construction have demonstrated in the past. I do not expect defense to lead a recovery because the reach of defense expenditures is so narrow. The rich get richer but the poor get nothing. For example, the Navy will spend 96 billion dollars over the next five years on new ships and refurbishing ships now in service. This work will be done in the Navy's own shipyards and in a relatively few commercial shipyards. Many yards, like Bethlehem Steel's Sparrow's Point (Maryland) and M-K's National Shipbuilding (San Diego) will run out of work in the absence of a commercial boom. Although defense provides work to prime contractors and a multitude of subcontractors, it is not sufficient to drive us out of a recession without the power of auto, highway construction, or home building.

"Once consumers are convinced that inflation is contained, they may start spending, and autos are logical candidates. Pent-up demand for housing exists now. Both housing and autos will influence capital expansion as defense and high tech never could."

Construction and Recovery

If there is a strong recovery in the construction industry, the same forces that have moderated wage increases could turn around. This would be especially true if a public-works program came into full activity at about the same time as capital spending spurred private construction. Professor Lewin offered this description:

"I expect to see a modest recovery in the construction industry in 1983. At the same time, and in part because of recovery, I also expect construction industry wages to rise more rapidly in 1983 than in 1982—say 8.0 to 8.5 percent compared to less than 7.0 percent. An increase in the demand for labor that is associated with 'producing' that good or service—and this is the scenario I envision for construction industry wages—will be tempered by (1) rising interest rates in the latter half of 1983, which will reduce the rate of growth in housing and commercial construction; (2) continued growth of the nonunion share of the construction industry, which now accounts for a majority of economic activity in this sector; (3) lags in the adjustment of collective bargaining and labor-market conditions to overall industry conditions and product demands; and (4) continued high unemployment for skilled workers in a variety of construction trades.

"All of this suggests a modest recovery in construction in 1983 *and* moderate increases in the rates of wage and labor costs, with the continued growth of the nonunion sector exercising a restraining influence on the unionized sector (and a continued narrowing of the gap between union and nonunion pay and benefits)."

Protection from Competition

As unemployment rose through 1982, there have been more special appeals for protection from imported manufactured goods "in order to save jobs." (It would not be effective to appeal for protection "in order to save higher prices.") Success at restricting imports has been achieved by the steel industry in 1982, and it plans further efforts in 1983. The auto union has proposed restricting the amount of imported components in cars sold in the United States. Mr. Neylan commented:

"Some legislators, at the behest of the auto companies and unions, are pushing domestic content legislation. The UAW claims that the legislation would save 800,000 jobs. (The Congressional Research Service estimates the saving to be 275,000.) Little thought has been given to the fact that the legislation would violate the General Agreement on Tariffs and Trade (GATT), which specifically prohibits domestic-content requirements. Steel has achieved a victory of sorts in its anti-dumping suits but imports from countries not involved, like Brazil, continue to come into our markets.

"The push for protection ignores the fact that our basic problem is that we have lost our monopoly position in many products. The push for domestic content in autos ignores the $65 billion that the auto industry has invested for the express purpose of recovering its competitive position in the domestic and international markets. I give auto-sponsored legislation little chance of passage.

"We no longer have a significant railroad passenger-car

industry, and purchases of Japanese and Canadian subway cars no longer make headlines. The Airbus created a flurry of excitement because of the subsidy implicit in its financing, but our leadership in commercial aviation is significant enough to mute the cries for relief. Our aircraft industry grew as a result of intense competition, has developed a clear technological advantage, and markets its product aggressively (unlike the smokestack industries).

"We have a strong position in semi-conductors, although the Japanese have now increased their worldwide market to about 35 percent. Japanese market focus on Europe, particularly in commodity memory devices, is a response to the suggestion of import quotas. I do not see broad- based support for protection in electronics. We have conceded the market in television, but the rest of the industry is simply too young and vigorous.

"Steel will continue aggressively pursuing its antidumping activity in a vain attempt to secure its market position. Unfortunately, in commodity products most efficient foreign producers have no need to dump since they can probably compete directly in this market. Steel's future lies not in tariffs but rather in rationalizing its output by shelving inefficient capacity and concentrating on specialty products. In summary, I suggest that protectionist legislation will not pass but I would expect renewed activity for 'voluntary limitations' on specific products—auto and steel in particular."

Mr. Winpisinger comes down squarely in favor of protection in heavy industries:

"Current legislative developments indicate the least we can expect in the way of protection of U.S. markets and workers is some degree of 'content' legislation for industries that have been hardest hit by foreign imports. And it is about time. The United States has been playing patsy to the rest of the world ever since the end of the Second World War. We have given other countries easy access to our markets while they have erected a wide range of direct and indirect barriers to stop our goods at their borders.

"When Japan takes direct aim at our semi-conductor industry (as it has), or France decides to try to knock the U.S. aerospace industry out of the air (as it has), this is not free competition. This is a matter of governments subsidizing every aspect of planning, financing, production and sales. Even a company as well managed as Boeing does not have the resources to compete against a French aircraft industry subsidized and backed by the French government. At some point, our government is going to have to provide the same kind of support and protection to industries and workers that are being bankrupted by this kind of competition.

"All of the industries mentioned—that is, autos, transportation, machinery, electronics and steel—are essential to the future of this nation. All are being systematically destroyed today. If we intend to have the capability to defend ourselves (and the rest of the so-called 'free world'), it is time to start thinking about where the next generation of skilled craftworkers will come from, once these industries are allowed to go down the drain.

"While it is incredible that our once great machinery and machine-tool capability is being destroyed by imports from Japan and Europe, it is even more incredible that our military is becoming increasingly dependent on sensitive military equipment produced in Korea and Japan.

"Some of the jobs that will never be regained are in industries that are being wiped out by competition subsidized by foreign governments—autos, steel, shipbuilding, machine tools."

However, Mr. Winpisinger is not willing to place all the blame for steel's weakness on the subsidies accorded foreign producers:

"The real issue here is whether the workers should have to pay for steel management's 20 years of failure to modernize. The steel industry's inability to compete with more modern, government-subsidized, foreign manufacturers is largely due to its own shortsightedness.

"These companies now blame their plight on wages. But what do they want? Surely it is not realistic to believe wages in the United States can be reduced to the levels paid in Taiwan, Korea or Mexico. Such wage differentials have always been there. In the past they were a source of national pride because we had a technologically advanced industrial base. If that is no longer true, it is not labor's fault."

Daniel Mitchell expects a "pro-market" philosophy in the Administration to prevent a rise in legislated protections. But an Administration that listens carefully to the requests of individual business leaders may respond with informal help against import competition.

"Pressures for import limitations have historically accompanied high unemployment. The Smoot-Hawley Tariff increases of the early 1930's are a prime example. However, the trend in the post-World War II period has been to put more and more authority over tariffs and other trade barriers in the hands of the President. Since the Reagan Administration opposes trade barriers, its opposition is a powerful force limiting the chances for such measures.

"However, it is possible for pressures to develop at the margin for trade barriers through informal arrangements that avoid formal legislation and rule making. The limits on auto imports from Japan are an example. There may be more pressure for 'temporary' agreements to hold down imports. Steel has had some success along these lines in the past."

Mr. Clem, speaking of the steel industry, makes a distinction between legislated protection (tariffs and/or quotas) and "voluntary restriction" by exporting countries:

"We hope that the government continues to oppose unfair trade practises, such as dumping. In our opinion, a forceful, unfair, protection effort will ultimately result in